SUSTAINABLE INVESTMENT: TRANSPARENCY, CLARITY AND TRUST

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Good morning. And thank you Carlos for your kind words of introduction.

It is a real pleasure for me to participate in this presentation of the Funcas study. I would like to thank Funcas and CECA for inviting me and take this opportunity to acknowledge the work that both institutions carry out in the field of disseminating economic analysis.

Today's report rightly goes deeper into the study and dissemination of sustainable finance. And, in particular, into the need to develop financial instruments and products to finance the energy transition.

Meeting the climate targets of the Paris Agreement requires significant efforts to transform business and our consumption habits. And this transformation requires high volumes of financing. The European Union, as announced in the Green Deal investment plan, aims to mobilise up to one billion euros of sustainable investments in the next decade[1].

As the Funcas report points out, one of the key elements necessary for this objective to be met is to have a clear and consistent regulatory framework.

Today I would like to make a brief reflection on the regulatory framework applicable to this area and the role of the CNMV as securities supervisor. Furthermore, I shall also speak in detail about the new sustainability reporting requirements which particularly affect investment funds, and in general, the asset management sector.

The Paris Agreement was ratified by the EU in October 2016, more than four years ago. Since then, multiple initiatives and policies have been launched in Europe to accelerate the transition to a low-carbon economy[2].

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[1] *The European Green Deal Investment Plan*, January 2020. The ultimate goal is to reduce greenhouse emissions by 55% by 2030 and achieve climate neutrality by 2050, thereby meeting the climate targets of the Paris Agreement.
[2] Such as the EU's March 2018 Action Plan for Financing Sustainable Growth or the 2019 Green Deal.

From a market supervisor's point of view, what elements are important in the regulation of sustainable finance? In my opinion, regulation should:

- help companies manage their climate risks and finance their business transformation;
- provide the necessary information to investors, so that they can compare and have reliable information about the risks and the type of exposure they are taking on;
- and enable the development of new financing instruments, such as green bonds or social bonds, and new ways of channelling savings, such as sustainable investment funds.

In short, a framework that enables the development of sustainable finance on the basis of clarity, reliability and comparability of information. To give confidence to the investor and avoid the risk of greenwashing.

The progress made by European public authorities has been remarkable. We now have a taxonomy[3] which, although it is not yet complete, provides the basis for classifying sustainable economic activities across the EU. The taxonomy recognises as green, or environmentally sustainable investment those activities that make a substantial contribution to at least one of the six climate and environmental objectives it defines, while not significantly harming any of them[4]. It thus provides a key benchmark for determining the degree of sustainability of an economic activity.

There are several aspects of the taxonomy awaiting development. Therefore, the technical selection criteria for the different objectives have not yet been defined, nor have the details of the new reporting obligations that the taxonomy regulation introduces by amending existing legislation such as the Non-Financial Reporting Directive. The development of a social taxonomy, among other aspects, is also being studied. Similarly, work is being done to prevent the classification of activities from being too binary, which would make it possible to take into account economic activities that, without complying with the strictest sustainability criteria, contribute to facilitating the necessary transition towards a more sustainable economic model[5].

That said, despite regulatory progress, we still have some way to go.

In recent years, in the absence of a comprehensive framework, the private sector has taken the lead. Investors and institutions have developed standards and principles to respond to a growing market demand. The work done is commendable and is in fact serving as a basis for the development of standards in areas such as non-financial information or the issuance of instruments.

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[3] Regulation (EU) 2020/852, of 18 June 2020, on establishing a framework to facilitate sustainable investments.

[4] In addition, they must be carried out in accordance with minimum guarantees with respect to human and labour rights and must comply with the technical selection criteria that the EC will establish by means of delegated acts, which are still pending approval.

[5] In this regard, it is worth noting the report published by the Sustainable Finance Platform - the expert group established to advise the European Commission - for the development of a transition taxonomy *(Transition Finance Report*, March 2021).

But it is also true that the lack of homogeneity and common criteria has led, in some cases, to an excessive plurality of methodologies and frameworks, and to an increasing difficulty in comparing the information published by companies.

This gives rise, for example, to situations in which the same company or issuer may receive a completely different environmental rating[6] depending on the agency awarding it. Recent estimates show that while in traditional credit quality ratings the correlation between the ratings given by different agencies to the same issuer is very high, close to 99%, this drops to 60% in the case of environmental or ESG ratings[7]. The different methodology, the information used, or the type of framework chosen by the company to prepare its non-financial information are some of the factors that explain this disparity. In fact, the European Securities and Markets Authority, ESMA, published last January a letter to the European Commission pointing out the need for the regulation of ESG ratings and valuation tools[8].

Progress on common regulation is therefore a priority. And for a supervisor such as the CNMV, it is a growing need. This is why sustainable finance is going to be one of the pillars of our strategy for the coming years. As stated in our Activity Plan, we are committed to working to facilitate the role of the securities market in the transition to a more sustainable and inclusive economy, ensuring the reliability of investor information. Our role is not to steer investments towards sustainable products, but to ensure that the right framework is in place for companies and investors to make informed decisions, and thereby advance the transition.

New reporting and transparency obligations on sustainability in investment services

Next, I would like to focus on the new transparency obligations on sustainability that apply to the investment services sector. These obligations have been applicable since 10 March past, as a result of the direct application of the European Disclosure Regulation[9].

In the area of the CNMV, the new requirements affect management companies and financial advisers, as well as certain investment products and funds.

Therefore, the entities bound by the Regulation, including investment fund managers, must report in two complementary areas:

- On the one hand, as an entity, they have to report, among other aspects, on how they integrate sustainability risks into their investment decisions and remuneration policies. And also on the main adverse impacts that their investment decisions may have on sustainability factors.
- And on the other hand, with regard to the investment products and funds they market, they must provide additional detailed information in those cases in which the fund manager declares that the fund promotes environmental or

[6] Ratings by ESG (environmental, social and corporate governance) criteria.
[7] See "*ESG ratings: Status and key issues ahead*", ESMA Report on Trends, Risks and Vulnerabilities No. 1, 2021.
[8] https://www.esma.europa.eu/press-news/esma-news/esma-calls-legislative-action-esg-ratings-and-assessment-tools
[9] Regulation (EU) 2019/2088, of 27 November 2019, on sustainability-related disclosures in the financial services sector (SFDR).

social characteristics (as per to article 8, also known as light green), and in those cases in which it is declared that the fund has sustainable investments as its objective (pursuant to article 9 or dark green).

However, the lack of clear definitions at European level means that implementation will not be simple, neither for institutions nor for supervisors, as we are awaiting the regulatory developments that will establish the technical selection criteria[10].

In order to facilitate compliance with the new obligations in the Spanish market, we at the CNMV have taken a two-pronged approach:

- On the one hand, we have announced[11] that we will carry out our work in a flexible and proportionate manner in monitoring compliance with the new obligations. Thus, we will seek to apply harmonised criteria at European level, following the guidelines determined by ESMA, and we will disseminate criteria, in the form of questions and answers, to clarify the queries received as a result of the continuous contact we maintain with the entities. In addition, we have established a simplified procedure to facilitate the updating of investment fund prospectuses. Currently, 85% of the managers have already submitted the documentation and I would encourage the remaining ones to make use of this facility. The aim is for the Spanish sector to adapt in a timely manner to the new requirements.

- Furthermore, we have to make sure that this flexibility that we give does not undermine investor protection. To this end, it is necessary to establish minimum reporting and transparency requirements, while awaiting the developments that will establish the final criteria.
    - Thus, investment funds that declare that they promote sustainability (art. 8) must explain the factors they promote, describe the type of strategy and indicate, inter alia, the minimum percentage of investments used to achieve the environmental or social characteristics promoted.
    - In the case of funds that declare themselves as sustainable funds (art. 9), they must also indicate the sustainable investment objective they pursue, their strategy and the percentage of the portfolio allocated to sustainable investment or the sustainability indicators they use to measure the achievement of the sustainable investment objective.

Similarly, to avoid the risk of greenwashing and to avoid confusing potential investors, the use of sustainable terms (or ESG factors) in the name of the investment fund should be restricted to those that meet minimum requirements. For example, an investment fund that allocates less than 50% of its investments to promoting sustainability should not use ESG terms in its name. The use of environmental terms in advertising and commercial communications should also be adjusted to the characteristics of the fund in question.

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[10] The development of the Regulation that will establish the criteria, known as level 2, is still pending approval, although there is a draft RTS.

[11] See the CNMV public statement on the forthcoming implementation of Regulation 2019/2088 on sustainability disclosures in the financial sector, also following the criteria and recommendations of the ESAs *Joint ESAs Final Report under SFDR*.

Overall, the Spanish investment services industry is well prepared to face the new demands, and has made a great effort to adapt. Currently, we already have around 60 funds registered that the fund manager declares that it promotes sustainability and one fund with a sustainable investment objective. And the trend is growing. Another 64 are in the process of updating their prospectuses as promoters of sustainability and an additional nine as sustainable funds. In total, it is likely that in the short term we will have just over 130 investment funds declaring that they promote or have sustainability as their objective.

In the coming months we all have to make an extra effort to adapt to the requirements that will come, both the industry and the CNMV, in its role as supervisor. And in this area, we can spare no effort in explaining to investors what sustainable investments are and the principles they promote. After all, good understanding and transparency are the basis for building trust in the new environment. The risk of selling as green what is not is no small matter, and avoiding it benefits all parties concerned.

I shall finish by saying that we expect a lot of regulatory activity this year in the area of sustainable finance. The EC will presumably publish its Renewed Sustainable Finance Strategy in June. In addition, in the coming months, we are awaiting, among others, the publication of new regulations establishing a European standard for the issuance of green bonds, an eco-label for financial products, the reform of the Non-Financial Reporting Directive and the EC delegated acts with the technical criteria for the selection of the taxonomy.

All of this will undoubtedly contribute to and enable the creation of the orderly framework to which I referred at the beginning. A framework that facilitates the development of sustainable finance on the basis of transparency and reliability of information, thereby generating sufficient investor confidence and protection.

Thank you for your attention.